SUPREME COURT, U. S.

FILED

JUN 12 1967

JOHN F. DAVIS, CLERK

IN THE

Supreme Court of the United States

Term, 1967.

No. 240

ARKWRIGHT MUTUAL INSURANCE COMPANY
(Plaintiff-Appellant in the Court Below),
Petitioner,

v.

BARGAIN CITY, U. S. A., INC.,
Respondent.

Petition for Writ of Certiorari to the United States Circuit Court of Appeals for the Third Circuit.

GEORGE E. BEECHWOOD,
BEECHWOOD & LOVITT,
Attorney for Petitioner.

Chester Springs, Pa.
1530 Locust St.,
Philadelphia, Pa.

International, 711 So. 50th St., Phila., Pa. 19143—Tel. SA 7-8711 Area Code 215

INDEX.

	Page
MOTION FOR LEAVE TO FILE PETITION FOR WRIT OF CERTIORARI	i
PETITION FOR WRIT OF CERTIORARI	1
Jurisdiction	2
A. Questions Involved	3
B. Federal Statutes Involved	3
C. State Statutes Involved	3
D. Statement of the Case	4
E. Facts	5
F. Reasons for Granting the Petition	12
The Court Sitting in Bankruptcy Lacked Summary Jurisdiction to Deal With the Claim	19

TABLE OF CITATIONS.

Cases: Page

Barnes v. Alexander, 232 U. S. 117 18
Bridge et al. v. Kedon, 163 Cal. 493, 126 Pacific 149 23
Cline v. Kaplan, 323 U. S. 97 .....12, 20
F. A. R. Liquidating Corp. v. Brownell, 209 F. 2d 375 (1954), C. A. 3rd 14
Gladowski, et al. v. Felczak, 346 Pa. 660, 31 A. 2d 718 (1943) 16
Grayson, et al. v. Securities, et al., 320 F. 2d 940 (1963) 27
Hurley v. Ashbridge, 55 Pa. Super. 523 (1914) 15
In re Borok, 50 F. 2d 75 (2d Cir. 1931) 13, 20
In re Commonwealth Bond Corp., 77 F. 2d 308 (2d Cir.) 18
In re Eakin, 154 F. 2d 717 (2d Cir. 1946) 13, 20
In re Interborough Consol. Corp., 288 F. 334 18
In re Sussman, 289 F. 2d 76 (3rd Cir. 1961) 13, 21
In re Walter & Sons, Inc., 10 F. 2d 463 (3rd Cir.) 19
Inter-State National Bank v. Luther, 221 F. 2d 382 (10th Cir. 1955) 13, 21, 23
Prudence Bond Corp., 79 F. 2d 215 19
Sexton v. Kesseler, 255 U. S. 90 (1912) 17
Taylor v. Sternberg, 293 U. S. 470 .....12, 20
Wells v. Wells, 166 Pa. Super. 634, 74 A. 2d 702 (1950) 16

Authorities:

9 Am. Jur. 2d Bankruptcy Sec. 902 19
9 Collier on Bankruptcy, Sec. 801 19

Statutes:

Bankruptcy Act, 11 U. S. A., § 110(c), § 2(a)(7), § 11(a)(7) 3, 12, 18, 20, 22, 23
Military Claims Act, 19 U. S. C., Sec. 2731 et seq. 3, 13, 21
Pennsylvania Uniform Commercial Code, 12A P. S. (Pocket Part) § 9, 102(1), 203, 301(3), 302, 303 ..... 3, 14
Supplemental Appropriations Act 1963, 77 Stat. 20 et seq. 12, 20

IN THE

Supreme Court of the United States

No.

TERM, 1967.

ARKWRIGHT MUTUAL INSURANCE COMPANY
(PLAINTIFF-APPELLANT IN THE COURT BELOW),
Petitioner,

v.

BARGAIN CITY, U. S. A., INC.,
Respondent.

MOTION FOR LEAVE TO FILE PETITION FOR WRIT OF CERTIORARI.

To the Honorable, the Chief Justice and Associate Justices of the Supreme Court of the United States:

And Now, to wit, this 10th day of June 1967, comes the petitioner by its Counsel, George E. Beechwood, a member of this court, and moves this Honorable Court to grant the petitioner, Arkwright Mutual Insurance Company, leave to file a petition for Writ of Certiorari with this Court.

GEORGE E. BEECHWOOD,
Attorney for Petitioner.

IN THE

Supreme Court of the United States

No.

TERM, 1967.

ARKWRIGHT MUTUAL INSURANCE COMPANY
(PLAINTIFF-APPELLANT IN THE COURT BELOW),
Petitioner,

v.

BARGAIN CITY, U. S. A., INC.,
Respondent.

PETITION FOR WRIT OF CERTIORARI.

To the Honorable, the Chief Justice and Associate Justices of the Supreme Court of the United States:

The petition of the Arkwright Mutual Insurance Company hereinafter referred to as petitioner, respectfully represents:

This is a petition for a writ of certiorari to the United States Circuit Court of Appeals for the Third Circuit to review the Decree of the United States District Court for the Eastern District of Pennsylvania, 251 F. Supp. 221 (E. D. Pa. 1966), affd., 373 F. 2d 701 (3rd Cir. 1967).

Petition for Reconsideration was denied on March 13, 1967.

The Opinion of the District Court is printed in Appellant's Appendix at pages 157a-170a.

The Opinion of the United States Court of Appeals is appended hereto.

The Order of the Circuit Court sur Petition for Rehearing is appended hereto.

JURISDICTION.

Jurisdiction is based upon Diversity of Citizenship. Petitioner is a corporation of the State of New Hampshire with its principal office in the State of Massachusetts. The Respondent is a corporation of the Commonwealth of Pennsylvania with its principal office in the Commonwealth of Pennsylvania. The amount in controversy is $100,000, a liquidated sum.

A. QUESTIONS INVOLVED.

1. Was the respondent unjustly enriched at the expense of the petitioner?

2. Did the petitioner have an equitable lien against the $100,000.00 deposited in the Registry of the District Court by the order of the Court?

3. Was it error for the District Court to hold that:

(a) no constructive trust arose upon the fund in favor of the petitioner;

(b) petitioner's security interest had to be perfected under Pennsylvania's Uniform Commercial Code.

4. Was it error for the Circuit Court to hold that the petitioner had an equitable lien, but the Court would not enforce same because petitioner failed to present that claim (which was and is factually incorrect) in the arrangement proceedings under Chapter XI?

5. Was it error for the Circuit Court to deny the petitioner the right to a trial of any kind, whether by jury or otherwise, with respect to disputed facts assumed to be true by the Circuit Court and upon which the Circuit Court based its dispute? Mental theft is not an excuse for robbery. It is hoped that this Court will not subscribe to such a principle.

B. FEDERAL STATUTES INVOLVED.

1. Military Claims Act, 19 U. S. C. § 2731, § 2733D.

2. Bankruptcy Act, 11 U. S. A., § 110(c), § 2(a)(7), § 11(a)(7).

C. STATE STATUTES INVOLVED.

1. Pennsylvania Uniform Commercial Code, 12A P. S. (Pocket Part) § 9, 102(1), 203, 301(3), 302, 303.

D. STATEMENT OF THE CASE.

On October 4, 1960, the petitioner issued its insurance policy insuring Bargain City, U. S. A. Inc. against damage for loss of rental property (56a and 58a).*

On August 27, 1961 a jet aircraft owned by the United States of America and operated by the personnel of the navy of the United States of America crashed into the premises of the petitioner's property causing a loss of rental income in excess of $100,000.00. After due and proper consideration the respondent made claim against the petitioner by reason of said insurance policy. It appeared by reasonable diligence that the respondent's damages, as a result of the jet aircraft smashing the respondent's premises, exceeded $100,000.00 and exceeded limits of the petitioner's policy.

The respondent desired to present and pursue its claim against the Government of the United States. In the meantime the respondent was pursuing its gross claim for damages against the Government of the United States. The respondent wished to obtain from the petitioner an advancement in the nature of a loan of $100,000.00.

The respondent did in fact receive an advancement of $100,000.00. A receipt and an agreement reciting the facts with respect thereto were executed (13a to 18a).

In addition there was in fact issued and delivered by the respondent on March 23, 1962, a Loan Receipt which provided:

> "Received from Arkwright Mutual Insurance Company the sum of One hundred thousand 00/100 Dollars as a loan, without interest, under Policy No. 115123 Rental Inc., repayable only in the event and to the extent that any net recovery is made by Insured from any person or persons, corporation or corporations, or other par-

---

* The letter "a" refers to appendix printed separately.

ties, on account of loss by fire, sprinkler leakage, or other casualty for which such insurance company may be liable under Policy No. 115123 occasioned to insured property on or about the Twenty-seventh day of August, 1961.

"As security for such repayment, we hereby pledge to said Arkwright Mutual Insurance Company whatever recovery we may make, and deliver to it herewith all documents necessary to show our interest in said property and we hereby agree to present claim promptly and, if necessary, commence, enter into and prosecute suit against such person or persons, corporation or corporations, through whose negligence the aforesaid loss was caused, or who may otherwise be responsible therefor, with all due diligence in our own name, but at the expense of and under the exclusive direction and control of the said ARKWRIGHT MUTUAL INSURANCE COMPANY." (74a)

The English language is clear and precise

"As security for the repayment we hereby pledge . . . whatever recovery we may make and deliver herewith all documents necessary to show our interest, etc. . . .".

Pledge "as security" means exactly what it states.

The petitioner wishes its right to property to be determined by a Federal Judge.

E. FACTS.

Representatives of respondent met with officials of the Department of the Navy, following which the Under Secretary of the Navy addressed a letter to the Director, Bureau of the Budget, Washington, D. C., dated April 23, 1962 and reported the claim of the Bargain City, U. S. A. by

reason of said jet crash in the sum of $228,404.34, comprised of $156,000.00 loss of profit (U & O) and $72,404.34 damage to store fixtures (47a).

Following the recommendation of the Navy, bills appropriating funds in payment of respondent's damages were passed by both the House of Representatives and the Senate of the United States (47a). Appropriation bills which included the exact amount of items referred to above were submitted to "conference" and later passed the House of Representatives and Senate and enacted into law (47a, 48a).

On October 19, 1962 respondent filed a Petition with the Clerk of the United States District Court for the Eastern District of Pennsylvania proposing an Arrangement under Chapter XI of the Bankruptcy Act of the United States (48a, 114a). Respondent filed with its Petition a schedule designated A-3 and upon which was typed on page 1 thereof, the following:

> "All creditors' claims are on open account *except where otherwise indicated.*" (Emphasis supplied.)

On page 8 of Respondent's Schedule (A-3) under the Chapter XI proceedings, petitioner was listed as a creditor on an open account, in the amount of $5,764.65 (48a, Pl. Rq. 20, Df. Ad., 113a [1]).

No asterisk or indication otherwise appeared in connection with said listing of petitioner as a creditor on an open account in the amount of $5,764.65 (Pl. Rq. 21, 48a).

On page 9 of Schedule A-3, petitioner is listed in the amount of $100,000.00. Preceding the word "Arkwright" there is typed an "asterisk" designating that petitioner was a party listed otherwise than as a creditor on an open account. Immediately following the listing of petitioner with an asterisk is the explanation:

---

1. Pl. Rq. designates plaintiff's Request for Admissions and Df. Ad. designates defendant's Admissions.

"'*ADVANCE RE: HORSHAM AIRPLANE CRASH CLAIM AGAINST U. S. NAVY.'' (Pl. Rq. 23, 49a, 114a (B))

In respondent's section C of Schedule B-3 in the Chapter XI proceedings, it appeared then and now appears as follows:

"Claim against U. S. Navy Department arising out of Navy airplane crash at Store #10, Horsham, Pa. on August 27, 1961. Claim adjusted, but not yet covered by Congressional appropriation." (Pl. Rq. 24, 49a, Df. Ad. 113a)

The respondent's original Schedule filed with the Petition for an Arrangement under Chapter XI of the Bankruptcy Act was and is on file with the Clerk of the United States District Court for the Eastern District of Pennsylvania (49a).

No other list of creditors with different designations or exceptions with respect to petitioner was filed by the respondent or its counsel prior to or immediately following March 12, 1963 other than those set forth above.

Petitioner did not receive notice of any kind of any proceedings relating to Bankruptcy Docket, Chapter XI, Cause No. 27505 in the matter of Bargain City, U. S. A., Inc., a corporation, until three months after the filing of said Petition for Arrangement, namely—January 23, 1963.[2]

The Plan of Arrangement of respondent was approved by Referee Curtin on March 12, 1963 and approved by Judge Wood and the management of respondent was turned over to its Officers and Directors effective as of March 12, 1963.

On March 18, 1963 Mr. Jaffe and a Mr. Lawrence G. Horowitz called upon Mr. Jacks to work out the mechanics of the procedure by which petitioner would receive the $100,000.00 advance pursuant to the Agreement, and

2. Disputed.

whereby respondent would immediately receive the balance as and when the Government issued its check.[3]

On March 20, 1963 Mr. Jaffe, through a telephone conversation agreed with George E. Beechwood among other things:[3]

> (a) that as and when the Navy Department pursuant to an Act of Congress received a check from the Government Disbursing Officer in payment of said claims of respondent that petitioner would agree mutually with respondent that the Navy retain said check until such time as Mr. Beechwood, together with properly and duly authorized officers and attorneys for respondent, could go to Washington, D. C. and obtain said check from the Government;
>
> (b) Petitioner would draw a check to the order of respondent in exchange for respondent endorsing the check of the Government directly to petitioner. The amount of petitioner's check was to be that sum which would be equal to the amount of the government check covering U & O less the $100,000.00;[3]
>
> (c) Respondent would furnish the manpower (two officers authorized to sign) to go to Washington, D. C. so as to properly endorse said check of the Government to the order of petitioner.[3]

Albert J. Feldman, Esquire, was counsel for the respondent from October 19, 1962 up to and including March 12, 1963.

Mr. Feldman did not at any time suggest that petitioner was an unsecured creditor as to the said $100,000.00. On the contrary Mr. Feldman and Mr. Criss openly asserted and acknowledged that the petitioner possessed a lien on the first $100,000.00. See affidavit of Ronald A. Jacks, Esquire,

---

3. Disputed.

a member of the Court for the District of Columbia and a member of this Court. The affidavit is dated June 6, 1967 appended hereto.

Mr. Jaffe, counsel for respondent, after March 12, 1963 freely admitted to Mr. Beechwood that Arkwright had an absolute right to the said $100,000.00. Such admissions continued until after April 4, 1963.[3]

On or about April 25, 1963 through the telephone Mr. Jaffe, in two separate conversations with Mr. Beechwood, as counsel for petitioner, suggested for the first time that there might be a question of petitioner's right to the said $100,000.00 because of the proceedings under Chapter XI.

Mr. Jaffe, in a letter dated May 7, 1963, took the position that petitioner had no right to the said $100,000.00.

On May 13, 1963 petitioner received at its office in Boston a printed form Note dated March 12, 1963 with the amount typed in as $15,000.00 payable to petitioner in 47 successive monthly installments. The said Note was not executed by the officers of defendant until on or about May 8, 1963.

On or about May 13, 1963 a check in the amount of $625.00 dated May 8, 1963 numbered 22454, payable to petitioner, was received by petitioner in Boston. Attached to said check was a paper containing the following typed information:

> "No claim filed. First installment $312.50, Second installment, $312.50. Amount payable, $625.00."

Said check No. 22454 was returned to respondent by letter. The said letter and the checks were delivered to respondent by mail at 800 Penrose Avenue, Philadelphia, Pennsylvania.

On Monday, May 20, 1963, less than thirty days after respondent had indicated it had intended to try to repudiate its written agreements petitioner filed a Complaint against the respondent in the above captioned matters requesting a

4. Disputed.

restraining order. A Restraining Order was granted on May 21, 1963 at 9:10 o'clock A. M., daylight saving time by the Honorable William Kraft, Jr.

On the 27th day of May 1963 petitioner and respondent, without prejudice to their respective positions filed of record a Stipulation.

On May 28, 1963, upon consideration of said Stipulation Judge Kraft, Jr. issued a Modified Temporary Restraining Order.

By letter dated June 4, 1963, Paul L. Jaffe, Esquire, forwarded to Captain W. J. Murphy, Assistant Director of Litigation and Claims Division, Washington Pentagon, Washington, D. C., a letter captioned re: Bargain City, U. S. A., Inc. (respondent).

On June 4, 1963 Paul L. Jaffe, Esquire, addressed a letter to George E. Beechwood re: *Arkwright Mutual Insurance Company v. Bargain City, U. S. A., Inc.* Said letter read as follows:

> "It would be appreciated if you would at your earliest convenience forward the form of release to be executed by Bargain City, U. S. A., Inc. as provided in the next to last paragraph of the Amended Temporary Restraining Order entered by Judge Kraft last week. By having this document delivered to me within the next day or so, I will be in a position to secure its execution and have it available for delivery as soon as the check or checks from the United States Government, which are the subject of the Order, have been received and delivered to the Clerk of Court."

A Release was prepared and executed by respondent on the 10th day of June, 1963.

Both petitioner and respondent filed pre-trial memoranda.

Petitioner filed motion for summary judgment on the whole record.

Petitioner's motion for summary judgment was argued on March 1, 1965 before the Honorable Judge Kraft.

On May 17, 1965, Judge Kraft filed an order suggesting insufficiency of proper allegations of jurisdiction in the Complaint.

On June 11, 1965, an Amended Complaint was filed. An Answer to Amended Complaint and New Matter was filed.

On October 12, 1965, the matter was re-argued before the Honorable Judge Kraft sur question as to whether or not the "rental income" became a part of defendant's estate for administration in the Chapter XI proceedings.

The Respondent did not file a motion for summary judgment. However, on December 8, 1965 there was filed of record a Stipulation between the parties wherein it was agreed that:

> "1. The Court may determine the issues herein as though the parties had filed cross-motions for summary judgment.
>
> "2. Petitioner is not a citizen of Pennsylvania and petitioner's principal place of business is in Massachusetts." (156a)

There was no agreement that the Trial Judge could substitute his version of undisputed facts, and interpret disputed facts into undisputed facts. Likewise there was no agreement that the Third Circuit could or should deprive petitioner of Due Process of Law.

The Trial Judge entered a final judgment in favor of the respondent, in the sum of $116,066.33, together with interest thereon from February 14, 1966, together with costs (172a).

F. REASONS FOR GRANTING THE PETITION.

It is of vast public importance that our Federal Courts lend their aid to correct the misappropriation of funds of a citizen of one state by a citizen of another state as originally contemplated by the founders of our Constitution and as supplemented by Congress.

The Circuit Court for the Third Circuit correctly struck down the reasoning of the District Court and then slid into the same result by equally improper reasoning and unsupported judicial reasoning to justify denial to the petitioner as against the respondent where a party has received payment twice—namely, the petitioner's $100,000.00 together with the Government's $100,000.00. There must be something wrong no matter how any Court may characterize it.

No language in the Bankruptcy Act specified in § 70, 11 U. S. C., § 110, nor does any case support the Third Circuit's conclusion.

The Bankruptcy Court had no jurisdiction over petitioner's property for purposes of administration under Chapter XI, and particularly is this true that it had no jurisdiction over the petitioner's property rights. Under all applicable statutes a lien is not subject to administration by anyone under the proceedings of Chapter XI. This is conceded by the Third Circuit. The United States Circuit Court for the Third Circuit gives this question the treatment of ignoring it.

See:

Cline v. Kaplan, 323 U. S. 97;
Taylor v. Sternberg, 293 U. S. 470.

Congress did not act in this matter nor did the law become effective awarding the respondent some $228,404.34 comprised of $156,000.00 loss of profit (U. & O.) and $72,404.34 damage to store fixtures (47a).

Supplemental Appropriations Act 1963, 77 Stat. 20 et seq.

That the Bankruptcy Court did not have possession and/or exercise its claim is definitely ruled in the cases of:

Barok, 50 F. 2d 75, 77 (2d Cir. 1931); and
Eakin, 154 F. 2d 717, 719 (2d Cir. 1946).

Also see

Inter-State National Bank v. Luther, 221 F. 2d 382, 386 (10th Cir. 1955);
Sussman, 289 F. 2d 76 (3rd Cir. 1961).

In the case at bar, when the petition under Chapter XI arrangement was filed in October, 1962 the debtor held a claim under the Military Claims Act, 19 U. S. C., Sec. 2731 et seq. This claim was not and could not have been paid by the Navy. The Navy's function is and was limited to investigating the claim and forwarding its recommendation to Congress for its "consideration". The Act provides, Sec. 2733(d) that:

"(d) If the Secretary of the military department concerned considers that a claim in excess of $5,000 is meritorious and would otherwise be covered by this section, he may pay the claimant $5,000 and report the excess to Congress for its consideration."

Congress, and Congress alone, had and is the final arbiter to decide whether such claims shall be paid and in what amount.

The reason why the Decree filed by the Circuit Court should be adjusted is within the language of the Opinion of the Third Circuit Court itself. That Court stated:

The following material facts are undisputed except where otherwise indicated."

That Court had no right to decide a case on cross-Motions for Summary Judgment on disputed facts, *F. A. R. Liquidating Corp. v. Brownell,* 209 F. 2d 375

(1954), C. A. 3rd, or to substitute false facts upon which to base a conclusion.

The District Court for the Eastern District of Pennsylvania, Kraft, J., struck down the equitable lien of the petitioner on the basis that the lien had not been perfected under the Pennsylvania Uniform Commercial Code, 12A P. S. (Pocket part) § 9-102(1), 203, 301(3), 302, 303.

On page 5 of the Opinion of the Third Circuit Court, Footnote 9, that Court correctly states:

> "We can find no method by which Arkwright could have recorded its interest. Contrary to the assertion of the appellee, the transaction was beyond the pale of the Uniform Commercial Code of Pennsylvania, which excludes from its scope 'a transfer in whole or part of . . . . any claim arising out of tort.' " 12A Pa. Stat. Ann. 9-104(k). See also 12 Pa. Stat. Ann. 9-104(g).

The question presents itself as to whether or not petitioner acquired an equitable lien upon payment by it to Bargain City, U. S. A., Inc., of the sum of $100,000.00 in March of 1962 (45a).

The indisputable and undeniable facts admitted of Record are that Bargain City received $385,106.30, $285,106.30 plus the $100,000.00 handed to it by the petitioner as against its total amount of damage of $285,106.30 (47a). If the law be that in equity petitioner had an equitable lien upon the happening of the event, to wit, the appropriation by Congress, to wit, of $228,404.34, and the receipt thereof by the respondent, the reasons for the District Court denying petitioner's relief having been declared erroneous, it remains only to determine whether or not the reasons stated by the Circuit Court are also equally erroneous. It has been tried to point out to this Court that petitioner had no right until, and only in the event, respondent recovered from the United States through an appropriation by Congress.

THE $100,000.00 RECOVERED BY RESPONDENT WAS IMPRESSED WITH A TRUST WHEN IT RECEIVED THE $228,404.43 FROM THE UNITED STATES.

The sum of $228.34 included the item of $100,000.00 which had been advanced by the petitioner to the respondent.

The Circuit Court in its Opinion indicates that the rights of the petitioner should be denied because of its non-active participation in the Chapter XI proceedings. If the lien was, in fact, an equitable one, contingent upon coming into being upon the happening of an event, it was not at the time of the proceedings, or anytime thereafter subject to any interdiction of the Chapter XI proceedings. On the other hand the Circuit Court stated:

> "Whether or not such a lien (equitable) arose is a question of state law, here that of Pennsylvania."

There appears to be no doubt that under Pennsylvania law the petitioner had an equitable lien enforceable upon the happening of the contingency, namely, the collection of the funds by the respondent.

The test for the creation of an equitable lien is that the parties intended to charge a particular fund with a specific debt and documents have been executed which clearly evidence that intention.

This doctrine has long been established in Pennsylvania. In *Hurley v. Ashbridge,* 55 Pa. Super. 523 (1914), plaintiff sought to establish and enforce an equitable lien on the basis of an agreement between the parties which provided that in return for an extension of time on his notes to plaintiff for labor and materials defendant would, in the event of sale (here the pledge as security of whatever recovery may be made from the United States):

> "pay the entire amount of said notes or any unpaid balance thereof out of the first proceeds of such sale

> and will immediately upon such sale give such order to Hurley [plaintiff] on the purchasers as will secure payment." [55 Pa. Super. 526].

On the basis of this document the Pennsylvania Court held that an equitable lien had been created. See pages 526-27 Id. where it is stated:

> 'It is agreed too that no particular form of words is required to create a pledge of a future fund or a lien thereon such as equity will recognize and enforce. It is sufficient if it plainly appears that the parties intended to pledge the fund and appropriate it to a particular purpose and have entered into some intention calculated to evidence and execute that intention."

See also *Wells v. Wells,* 166 Pa. Super. 634, 639, 74 A. 2d 702 (1950); *Gladowski, et al. v. Felczak,* 346 Pa. 660, 31 A. 2d 718 (1943).

No one has any quarrel that as between the situation of an injured property petitioner as against a citizen, person or corporation for the occurrence happening in Pennsylvania that the law of Pennsylvania would govern. No one has any quarrel with the statement as to whether or not a lien arose under ordinary circumstances was a question for state law, and here that of Pennsylvania. However, under Pennsylvania law an equitable lien arose under the decisions of the highest Courts of the State of Pennsylvania, and it is expected that this Court will follow the same if, in fact, such law is the governing factor. If it is, then, the petitioner had an equitable lien surviving the Chapter XI proceedings under Pennsylvania law.

It must be conceded that the law of the land of the United States of America exercised by the will of Congress was the law that was invoked and carried out.

This Court must note, if it applies Pennsylvania law, that the validity of an equitable lien is not impaired by the fact that the fund was not in existence at the time the agreement was executed. In Pennsylvania the lien will be enforced when and if the fund comes into existence. On the other premise as to whether or not the Federal law determines the existence of an equitable lien the petitioner stands firmly on either position. While the opinion of the 3rd Circuit Court states that the Pennsylvania law determines the question of a right to an equitable lien it is doubtful that Court followed Pennsylvania law. See the 2nd paragraph, page 7 of its Opinion. The 3rd Circuit quotes from the case of *Sexton v. Kessler,* 255 U. S. 90, 98-99 (1912), as stare decisis in support of its conclusion to deny the petitioner's right to an equitable lien. Thus, it is clear that that Court first states that the Pennsylvania law should be applicable in determining whether or not an equitable lien exists, and then turns to a statement in a decision of the United States Supreme Court, and only a part of that decision was and is relied upon to determine that the Pennsylvania law did not, in fact, apply.

There is something wrong (and the Circuit Court so agreed) that the Lower Court was in error in holding that the equitable lien failed because it had not been recorded under the Commercial Code of Pennsylvania. There is also something wrong when the Third Circuit states that the law of Pennsylvania governs equitable liens and then that Court fails to apply it.

Petitioner relies on either or both the law of Pennsylvania and/or the Federal law of the United States.

It is difficult to concur in the reasoning that active motions, petitions, hearings and other matters should have been filed in the bankruptcy court. Especially, is the pertinency of this observation all the more compelling when, in fact, under the Federal law the equitable lien never was within the bankruptcy proceedings, and a right in the peti-

tioner never existed until after the termination of the bankruptcy proceedings.

In *Barnes v. Alexander*, 232 U. S. 117, 121 (Holmes, J.), the Court said:

> "And it is one of the familiar rules of equity that a contract to convey a specific object even before it is acquired will make the contractor a trustee as soon as he gets a title to the thing."
>
> [This case involved the status of a contingent fee based on a percentage of the recovery.]

In re Interborough Consol. Corp., 288 F. 334, 349, the Court said:

> "But it is now definitely settled in the federal courts that a promise based on a consideration to pay out of a particular fund creates a lien on the fund, which attaches to the fund when it comes into existence and which equity will enforce, holding the promisor to be a trustee as soon as he gets title."

In re Commonwealth Bond Corp., 77 F. 2d 308 (2d Cir. L. Hand, Ct. J.), the debtor in reorganization proceedings under § 77(b) was a trustee for "certificate owners' having benefits and rights in certain real estate. The Court said, at page 309:

> "The trust property is not the debtor's property, the 'certificate holders' are not its creditors; no reorganization can include either . . . for the adjustment of a bankrupt's relations as fiduciary with its beneficiaries in the future is no affair of the bankruptcy court."

The Court went on to say:

> "Sub-division (a), § 77(b), 11 U. S. C., § 207(a) does grant jurisdiction over the debtor and its property wherever located but that gives no color to such power, for the trust property is *not the debtor's.*" (Italics supplied.)

In *Prudence Bond Corp.*, 79 F. 2d 215, the Court said:

> "If a trustee becomes bankrupt, the trust property is not administered in bankruptcy."

In re Walter & Sons, Inc., 10 F. 2d 463 (3rd Cir.), a shipper by contract agreed to pay to a Board of Commerce of which he was a member, a commission of 50% of all moneys received from railroads for freight overcharges to enable the Board to prosecute claims. Payments were to be refunded to members in proportion to amounts underwritten by them. The Court held that a recovery paid to a bankrupt shipper (member) was impressed with a trust in favor of the Board to the extent of 50% of the payment. The Court said:

> "The issue is the preservation of a trust fund . . . to enable the Board to fulfill its duty as trustee in the manner all parties, by their writing, agreed, when the Board was constituted their agent to raise these trust-impressed funds."

See also 9 *Am. Jur.* 2d Bankruptcy Sec. 902; 9 *Collier on Bankruptcy*, Sec. 801.

Since the respondent held its claim against the Government as trustee for the benefit of petitioner to at least $100,000.00, the petitioner's claim was not part of the estate in bankruptcy. Likewise, the proceeds of that claim to at least $100,000.00 was no part of the bankruptcy estate and the defendant, as trustee, is bound to pay this amount to petitioner.

Aside from this proposition, the bankruptcy court lacked summary jurisdiction to deal with the claim in any case.

The Court Sitting in Bankruptcy Lacked Summary Jurisdiction to Deal With the Claim.

The Bankruptcy Act provides that the trustee upon his appointment and qualification is vested by operation of law with the "title of the bankrupt" to the bankrupt's

property specified in Section 70 of the Act (11 U. S. C., Sec. 110). While this includes in a general way rights of action for injury to the bankrupt's property, a clear distinction is made between the trustee's right to recover in a plenary action against a third party and the right to deal with the claim under the Court's summary jurisdiction. The latter appears to be the question involved.

In order for the bankruptcy court to have summary jurisdiction over the debtor's property for purposes of administration under Chapter XI, the property must be in the actual or constructive possession of the debtor at the time the petition was filed. See *Cline v. Kaplan,* 323 U. S. 97; *Taylor v. Sternberg,* 293 U. S. 470.

It is clear that the bankruptcy court never had actual or constructive possession of the proceeds of debtor's claim against the Government since Congress did not award the sum until May 17, 1963, approximately two months after the plan was confirmed, the receivers discharged and the business returned to debtor, *Supplemental Appropriations Act 1963,* 77 Stat. 20 et seq.

While it is true as indicated above the receivers had the debtor's title to the claim or chose-in-action against the Government in the sense that the receiver could attempt to recover in a plenary suit on the claim against the Government, but no such plenary action was taken. In the absence of such plenary recovery, that claim is not subject to the summary jurisdiction of the bankruptcy court unless the third party (the Government) consents to such jurisdiction. Where such consent is not given or the claim is resisted, the chose-in-action is not in the "possession" of the bankruptcy court for summary jurisdiction.

Please refer to *In re Borok,* 50 F. 2d 75, 77 (2d Cir. 1931).

In re Eakin, 154 F. 2d 717, 719 (2d Cir. 1946), the Second Circuit held that a bankruptcy court did not have summary jurisdiction over funds in a bank deposit where the bank asserted the debtor deposited them as trustee.

> "But an action to enforce a debt from the alleged debtor of the bankrupt, where the debtor denies the existence of the debt, is not within the summary jurisdiction. The Trustee, in such a case, cannot claim possession, because the existence of the chose in action is the issue in dispute."

The Tenth Circuit in *Inter-State National Bank v. Luther,* 221 F. 2d 382, 386 (10th Cir. 1955), stated flatly that:

> "Everyone apparently concedes, as they must, that the bankruptcy court is without summary jurisdiction to adjudicate a controversy respecting property or chose in action held adversely to the bankrupt estate without the consent of the adverse claimant."

In re Sussman, 289 F. 2d 76 (3rd Cir. 1961), at the time of filing the petition, the bankrupt had a possible claim for refund of taxes against the Government based on a loss carry-back. The Court held that this was not part of the bankrupt's estate.

In the case at bar, when the petition under Chapter XI arrangement was filed in October, 1962 the debtor held a claim under the Military Claims Act, 19 U. S. C., Sec. 2731 et seq. This claim was not and could not have been conceded by the Navy. The Navy's function is limited to investigating the claim and forwarding it to Congress for its "consideration." The Act provides, Sec. 2733(d) that:

> "(d) If the Secretary of the military department concerned considers that a claim in excess of $5,000 is meritorious and would otherwise be covered by this section, he may pay the claimant $5,000 and report the excess to Congress for its consideration."

Congress and Congress alone is the final arbiter to decide whether such claims shall be paid and in what amount.

In the instant case, not even the first $5,000 was paid. Moreover, the parties themselves recognized that the Respondent's ability to recover from the Government was clearly in doubt. In fact, the agreement makes specific provision for the possibility that Congress might award Bargain City less than $156,000 or nothing at all.

> "5. In the event the United States shall pay less than the sum of $100,000 in settlement of Bargain City's claim for loss of rental, Bargain City shall forthwith pay to Arkwright an amount equal to the difference between the sum actually paid by the United States and $100,000; provided, however, that such repayment by Bargain City to Arkwright shall be without prejudice to the right of Bargain City to assert a claim under the policy in an amount greater than the sum paid by the United States, provided that the total amount of such claim shall not exceed $156,000.
>
> "6. In the event the United States shall pay less than the sum of $156,000, but more than $100,000, in settlement of Bargain City's claim for loss of rental the repayment of $100,000 by Bargain City to Arkwright as provided in Paragraph 2 above shall be without prejudice to the right of Bargain City to assert a claim against Arkwright under the policy in an amount greater than the sum paid by the United States but not in excess of $156,000."

In this context, until such time as Congress finally decided to pay petitioner's claim, the Government was in every essential fact an adverse claimant within the rule that limits the summary jurisdiction of the bankruptcy court. Thus, the court did not automatically acquire jurisdiction over that claim since its existence, i.e., its validity was the very issue in dispute.

Nor was summary jurisdiction conferred by "consent" of the Government. The question of implied consent is governed by amended section 2(a)(7) of the Bankruptcy

Act, 11 U. S. C. Sec. 11(a)(7) which provides in pertinent part:

> ". . . where in a controversy arising in a proceeding under this title an adverse party does not interpose objection to the summary jurisdiction of the court of bankruptcy, by answer or motion filed before the expiration of the time prescribed by law or rule of court or fixed or extended by order of court for the filing of an answer to the petition, motion or other pleading to which he is adverse, he shall be deemed to have consented to such jurisdiction."

Even a cursory examination of this provision indicates that before the question of an adverse party's implied consent can even be raised, there has to have been some affirmative action taken against him by the receivers or trustees. As the Tenth Circuit observed in *Inter-State National Bank v. Luther,* 221 F. 2d 382 (10th Cir. 1955):

> "When considered against the background of the considerations which prompted the amendment, we think it has application only to controversies arising in bankruptcy proceedings where the adverse party is brought into court by pre-emptory process, as in turn-over order cases like Cline v. Kaplan, supra; . . . ."

Since there was no such action by the receivers against the Government in this case, plenary or otherwise, there is no conceivable basis upon which the Government can be said to have given its implied consent to the summary jurisdiction of the bankruptcy court.

While the Third Circuit has not followed its own decisions or those of Ninth and Tenth Circuits, the decisions of the United States Supreme Court and the decisions of the highest Courts in Pennsylvania, nevertheless, one from California is quoted below in *Bridge et al. v. Kedon,* 163 Cal. 493, 126 Pacific 149, 152, 153.

"This being the nature of the equitable right created by the assignment, it would follow, in analogy to the rule concerning ordinary liens, that the discharge in bankruptcy did not divest Bridge of his then existing equitable right to Kedon's prospective inheritance. The general rule is well established that an assignment, invalid at law, but good in equity, is valid in equity against the assignor in bankruptcy, whether the thing is assigned absolutely or only as security for a debt. In the latter case, the discharge in bankruptcy terminates the legal personal obligation to pay the debt, and the right granted or assigned is limited to the enforcement of the payment of the money loaned, with interest, out of the property which is the subject of the grant or assignment. 3 Pam. Eq. Jur. § 1291; 5 Am. & Eng. Ency. of Law & Prac. p. 963. The assignment is treated in equity as a present contract to convey the future interest, a contract which creates a trust as soon as the interest becomes absolute; and this is a present existing right by contract, which the discharge in bankrupcty does not avoid or terminate. The continued existence of the debt as a personal obligation to pay money is unnecessary to the enforcement of an equitable charge or lien upon specific property. In Fletcher v. Morey, 2 Story, 555, Fed. Cas. No. 4,864; and Parker v. Muggridge, 2 Story, 345, Fed. Cas. No. 10,743, it was held that the Bankruptcy Act of 1841 excepted from its operation specific equitable liens and charges, as well as legal liens, and that an equitable charge could be enforced against the assignee in bankruptcy. This was put upon the ground that 'every such agreement for a lien or charge in rem constitutes a trust,' which binds the conscience of the assignor. It is said, further, that the act 'was by no means intended to affect any of the equitable liens or other equitable claims of parties, arising under their contracts,' and that 'the property will be followed and affected with the trust in the hands of the assignee [in bankruptcy]

in the same manner and to the same extent as it would be in the hands of the bankrupt.'

"The Bankrupt Act of 1898 expressly exempts from its operation and preserves all liens created by the bankrupt in good faith and for a valuable consideration more than four months before the filing of the petition in bankruptcy. Section 67, Bankrupt Act; 5 Cyc. 364. The act is in this particular identical with the Bankrupt Act of 1841 (5 Stat. 440, c. 9), and the above decisions apply to it with equal force. It is scarcely necessary to say that, if such an equitable charge in rem can be enforced against the assignor in bankruptcy, it must necessarily be enforceable against the bankrupt himself after his discharge, and especially in cases where the property which is subject to the charge did not get into the possession of the assignee, because at that time it had not been acquired by the bankrupt."

Thus, the bankruptcy court during the Chapter XI proceedings possessed no summary jurisdiction over the debtor's claim against the Government or the funds ultimately resulting therefrom, and was without power to determine the rights of appellant and appellee to the claim and therefore the claim was not part of the debtor's estate for administration in the Arrangement proceedings.

The Opinion of the Third Circuit summarizes its holding as follows:

"In summary, we hold that where a creditor claims a security interest which is at best equitable in nature, and fails to present that claim during arrangement proceedings of which it has notice and a reasonable time to do so, we will not, in the circumstances of this case, give effect to a claim for security which depends for its enforcement upon the equitable discretion of this court. The judgment of the United States District Court for the Eastern District of Pennsylvania will be affirmed."

The accuracy of this conclusion is incorrect and its effect deprives petitioner of due process.

The Loan Receipt was executed on March 23, 1962, the day on which the loan was made. It is set out in full at 17a and 18a. It reads as follows:

LOAN RECEIPT

V-298
Serial File
Dated March 23, 1962

$100,000.00 Rental Income

RECEIVED FROM ARKWRIGHT MUTUAL INSURANCE COMPANY the sum of One hundred thousand and 00/100 Dollars as a loan, without interest, Under Policy No. 115123 Rental Inc., repayable only in the event and to the extent that any net recovery is made by Insured from any person or persons, corporation or corporations, or other parties, on account of loss by fire, sprinkler leakage, or other casualty for which such insurance company may be liable under Policy No. 115123 occasioned to insured property on or about the Twenty-seventh day of August, 1961.

As security for such repayment, we hereby pledge to said Arkwright Mutual Insurance Company whatever recovery we may make, and deliver to it herewith all documents necessary to show our interest in said property and we hereby agree to present claim promptly and, if necessary, commence, enter into and prosecute suit against such person or persons, corporation or corporations, through whose negligence the aforesaid loss was caused, or who may otherwise be responsible therefor, with all due diligence in our own name, but at the expense of and under the exclusive direction and control of the said ARKWRIGHT MUTUAL INSURANCE COMPANY.

Bargain City, U.S.A. Inc.

By Walter O. Siler, Jr.
President

Attest: Myron Harris

(Corporate Seal)

The claim of the petitioner, Arkwright, had not ripened when the Chapter XI proceedings were being conducted. Furthermore, the lien, as indicated above, would not have been a proper item before the bankrupt court in the Chapter XI proceedings, even if the debtor had obtained Congressional action and the United States had, in fact, paid its claim. However, the fact is that the appropriation by Congress did not occur until after the Chapter XI proceedings had terminated and the rights of the petitioner could not arise, and did not arise, until after the respondent had, in fact, received the funds as trustee.

Please see *Grayson, et al. v. Securities, et al.*, 320 F. 2d 940 (1963).

For the above reasons this Court should grant a hearing to the petitioner.

Respectfully submitted,

BEECHWOOD & LOVITT,
By GEORGE E. BEECHWOOD,
Attorney for Petitioner,
Arkwright Mutual Insurance Company.